



*Andrew H. Junkin, CFA, CIMA, CAIA
Managing Director and Principal*

June 3, 2008

Ms. Anne Stausboll
Interim Chief Investment Officer
California Public Employees' Retirement System
400 Q Street
Sacramento, CA 95814

Re: MDP Program Review

Dear Anne,

You requested Wilshire's opinion with respect to Staff's performance review of the MDP program. Wilshire believes that MDP I and II are continuing to give CalPERS access to emerging firms in the investment industry. Although the performance of the MDP program has not met its benchmark, the Program is evolving and Staff now has greater control over the managers that will be selected.

Discussion

The MDP Policy states that the MDP program has 3 explicit goals: 1) Diversify CalPERS' overall equity program, 2) Enhance the expected return of CalPERS' investment program, and 3) Hedge against active member liabilities. More generally, MDP was designed to help CalPERS access emerging talent in the investment management industry. MDP I manager selection was controlled entirely by the MDP I Advisors, who sourced and funded investment management firms. MDP II granted Staff more control over the managers that would be selected and funded. Although MDP II is still a young program, giving Staff greater control over the types of strategies and firms that will be funded more closely aligns the intent of the program with the execution of the program.

In many senses, MDP is a difficult program to manage. Many talented managers are not interested in selling a minority interest in their firm. As such, the universe of candidates is fairly small. In fact, many emerging firms would prefer to work through an Emerging Manager Fund of Funds, where an external party simply funds new portfolios and does not demand an equity interest, which allows them to build up the firm's size without selling off an equity stake. CalPERS also invests in Emerging Manager Funds of Funds, thereby increasing the universe of emerging firms with which it can invest. However, CalPERS is, in effect, competing with its own MDP Program by investing with Emerging

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Funds of Funds, although, as discussed above, the MDP program and a Fund of Funds program have somewhat different investment opportunities.

The performance of the program has been mixed, with the venture portion of the program performing very well. However, the composite of underlying managers has underperformed its custom benchmark. In this case, giving Staff more control over the selection of the managers should improve the performance of the Program.

Conclusion

Wilshire believes that MDP is continuing to act as one avenue for CalPERS to find emerging, talented investment management firms. The structure of MDP II appears to be superior to MDP I and Wilshire would expect an improvement in the performance of the program as a result of those changes.

If you have any questions or comments, please let me know.

Sincerely,

A handwritten signature in black ink, appearing to read "Anne Stausboll". The signature is fluid and cursive, with a large loop at the end.